

Ahead of the Curve

January 25, 2019

We expect GDP to moderate to 2.0% yoy in 4Q18

- Gross domestic product (4Q18 P).** We expect 4Q18 GDP at 2.0% yoy, below the 2.5% of the previous quarter. Using seasonally adjusted figures, we anticipate 0.2% q/q growth, also lower than 3Q18 at 0.8%. This estimate is consistent with our annual GDP forecast of 2.1%. By components, we expect 2.3% yoy in primary activities (previous: 2.2%), -0.5% in industrial production (previous: +1.1%), while services could reach 3.1% (previous: 3.2%). In general terms, our estimate incorporates a series of signals suggesting a deceleration of economic activity in December, among them lower auto production and same-store sales, along reports of lower dynamism in global trade
- Trade balance (December).** We expect a US\$593.7 million deficit, more modest when compared to the previous month. In our view, oil exports could have been impacted by the extended fall in the price of the Mexican oil mix, while non-oil exports could have stood at 5.8% yoy. As a result, exports would grow 4.7%, which would be the second lowest print in 2018. Going to imports, we also expect a deceleration from 10.4% in November to 6.4%. Non-oil consumption goods will likely contract and intermediate- and capital- goods could show a more modest advance. If our forecast materializes, the trade deficit in 2018 would stand at US\$ 16,134.5 million, 47% higher than in 2017

 www.banorte.com
 @analisis_fundam

Juan Carlos Alderete, CFA
 Senior Economist, Mexico
 juan.alderete.macal@banorte.com

Francisco Flores
 Economist, Mexico
 francisco.flores.serrano@banorte.com

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Mexico weekly calendar

DATE	HOOR (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Mon 28-Jan	9:00am	Trade balance	December	US\$ mn	-593.7	--	-2,381.8
		Total exports		% yoy	4.7	--	2.8
		Oil exports		% yoy	-8.7	--	-4.5
		Non-oil exports		% yoy	5.8	--	3.3
		Total imports		% yoy	6.4	--	10.4
Tue 29-Jan	10:00am	International reserves	Jan-26	US\$ mn	--	--	175.0
Tue 29-Jan	12:30pm	Government weekly auction: 1-, 3-, 6-, 12-month CETES; 30y Mbono (Nov'47); 30y Udibonos (Nov'46); 5y Bondes D					
Wed 30-Jan	9:00am	GDP	4Q18 (P)	% yoy	2.0	--	2.5
		(sa)		% q/q	0.2	--	0.8
		Primary activities		% yoy	2.3	--	2.2
		Industrial production		% yoy	-0.5	--	1.1
		Services		% yoy	3.1	--	3.2
Wed 30-Jan	11:00pm	Budget balance	December	MXN bn	--	--	-351.0
Thu 31-Jan	10:00am	Comercial banking credit	December	% yoy	6.4	--	6.7
		Consumption		% yoy	1.6	--	1.7
		Housing		% yoy	4.6	--	4.7
		Non-banking private firms		% yoy	9.7	--	10.0
Fri 1-Feb	10:00am	Family remittances	December	US\$ mn	3,005.9	--	2,910.7
Fri 1-Feb	10:00am	Banxico's survey of economic expectations					
Fri 1-Feb	9:00am	PMI's survey (IMEF)	January				
		Manufacturing		index	48.5	--	49.3
		Non-manufacturing		index	49.0	--	49.4

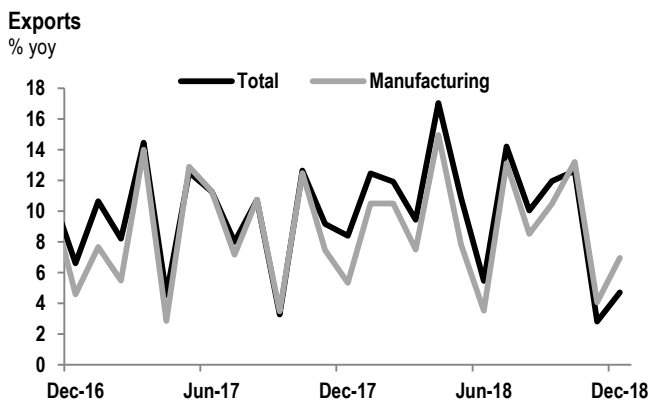
Source: Banorte; Bloomberg

Proceeding in chronological order...

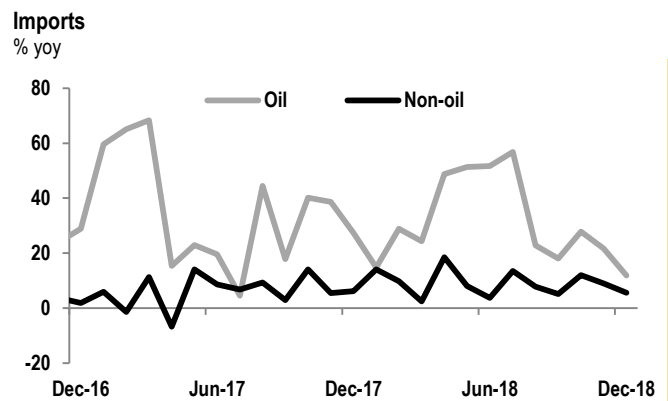
Trade balance could finish 2018 with a higher deficit than the previous year. We expect a US\$593.7 million deficit in December, more modest when compared to the -US\$ 2,381.8 million of the previous print. In our view, oil exports could have been impacted by the 18.3% m/m decrease in the Mexican oil mix, which came on top of the hefty 18% contraction of the previous month. As a result, the average price ended with its first year-on-year decrease since September 2016, at -7.9%. Considering this, we estimate oil exports to contract 8.7% yoy, below the -4.5% rate observed in November, when prices began to fall. On the contrary, non-oil exports would have accelerated to 5.8% yoy from 3.3%, expecting a slight pickup in autos after its recent batch of weakness. All in all, we expect exports to grow 4.7%, which would be the second lowest print in 2018 impacted by lower oil prices and the broad deceleration in global trade.

Going to imports, we expect a deceleration from 10.4% yoy in November to 6.4%. Oil-related imports would moderate their advance from 21.7% to 11.9%, while non-oil imports could also be more modest on signs of less dynamism in domestic demand. In particular, we expect consumption and intermediate goods to stand at -2.2% and +7.1%, respectively. Moreover, we forecast capital-goods at +1.5% from +6.8% in the previous month, with a significant deceleration due to the impact from higher uncertainty and low appetite for fixed investment among businessmen according to confidence data.

If our forecast materializes, the trade deficit in 2018 would stand at US\$ 16,134.5 million, 47% higher than in 2017. This would be mainly because of a widening oil deficit, from US\$ 18,308.7 to 23,825.3 million. It is worth noting that this has been due to surging oil-related imports, with an estimated balance of US\$ 54,612.9 million in 2018 (+30% yoy) and not because of lower oil exports, which will likely end higher in their annual comparison. On the other hand, this deficit would only be partially compensated by the increase of 4.8% in the non-oil surplus, expected to end at around US\$ 7,690.9 million.



Source: INEGI, Banorte



Source: INEGI, Banorte

Weekly international reserves report. Last week, net international reserves decreased US\$ 62 million, closing at US\$ 175 billion. According to Banxico’s report, this figure comes mainly from a negative valuation effect in central bank assets. In this context, the central bank’s international reserves have increased US\$ 237 million during 2019 (please refer to the following table).

Banxico's foreign reserve accumulation detail
US\$, million

	2018	Jan 18, 2019	Jan 18, 2019	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	174,793	175,029	-62	237
(B) Gross international reserve	176,384	178,190	818	1,806
Pemex	--	--	772	988
Federal government	--	--	99	861
Market operations	--	--	0	0
Other	--	--	-54	-42
(C) Short-term government's liabilities	1,592	3,160	879	1,569

Source: Banco de México

Weekly government bond auction. The Ministry of Finance (MoF) –via Banco de Mexico as its financial agent–, will offer 30-year fixed-rate Mbonos (Nov’47), 30-year inflation-linked Udibonos (Nov’46), 5-year Bondes D, in addition to the “more traditional” 1-, 3-, 6-, and 12-month zero-coupon Cetes (please refer to the following table). As usual, results will be released at 12:30pm (ET).

Auction specifics (Tuesday, January 29th, 2019)

	Maturity	Coupon rate, %	To be auctioned ¹	Previous yield ²
Cetes				
1m	28-Feb-19	--	5,000	7.91
3m	02-May-19	--	8,000	8.18
6m	01-Auo-19	--	10,000	8.40
12m	02-Jan-20	--	13,000	8.62
Bondes D				
12m	21-Dec-23	--	5,500	0.16
M Bono				
30y	07-Nov-47	8.00	3,700	9.12
Udibonos				
30y	08-Nov-46	4.00	UDIS 450	4.25

Source: Banorte with data from Banco de México 1. Except for Udibonos, which are expressed in UDI million, everything else is expressed in MXN million. 2. Yield-to-maturity reported for Cetes, Mbonos and Udibonos

Mexico’s preliminary GDP to moderate to 2.0% in 4Q18. On Wednesday, *INEGI* will publish its preliminary 4Q18 GDP report. *INEGI* uses the reports already published for the first two months of the quarter and estimates output for the third with the available information released so far. We forecast an economic expansion of 2.0% yoy, below the 2.5% observed in 3Q18. In addition, using seasonally adjusted figures we anticipate a 0.2% q/q growth, also below the 0.8% previously. Our estimate is consistent with our annual GDP forecast of 2.1%, albeit at the lower bound of the range.

During the first two months of the quarter, growth averaged 2.3% according to the monthly GDP proxy. Nevertheless, we expect broader weakness in December in the annual comparison, both in the secondary and tertiary sectors. The latter is due in part to a negative calendar effect in the month, particularly given that Christmas and New Year's Eve were on Monday, giving an additional incentive to employees to further lengthen their vacations. In contrast, in 2017 both of these were on a Sunday. On top of this, we have also seen some signs, both external and local, of a broader deceleration in activity.

By components, we expect 2.3% yoy in primary activities (previous: 2.2%), -0.5% in industrial production (previous: +1.1%), while services could reach 3.1% (previous: 3.2%). Within industrial production, we highlight a deceleration in manufacturing output, with early data in December pointing to additional weakness in auto production, falling 9.7%, which had not been seen since the financial crisis –excluding months in which the *Holy Week* took place-. Moreover, industrial production in the US has provided mixed signs. Although hard data remain relatively strong, the forward-looking ISM manufacturing declined significantly. The Mexican peso strengthened, which tends to negatively impact exports. Mining activity will continue to drag down production as the oil production platform continues to fall.

Regarding services, we have also seen weaker performance at the margin. In particular, ANTAD's same-store sales declined 1.4% yoy in real terms (lowest since April) while vehicle-sales fell 10.6%. Considering the latter, we anticipate a relatively strong deceleration in retail sales during the last month of the year, although the quarter would still be supported by resiliency in the previous months (average of 3.2%). Last but not least, weakness in manufacturing could also have had an impact on transportation, more so considering that the first delays in fuel distribution could have taken place at the end of the month in some states.

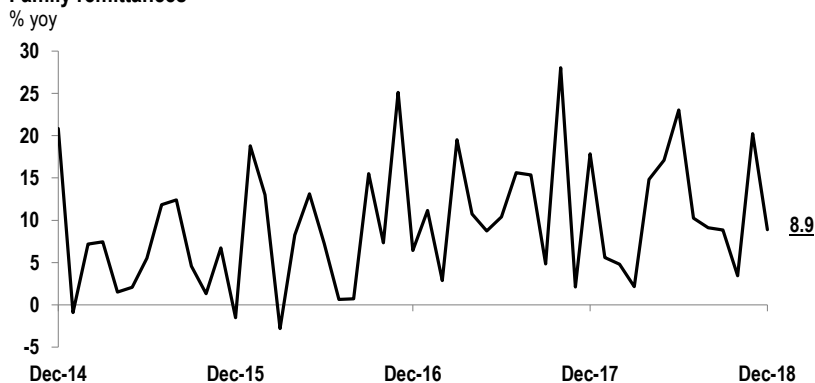
MoF's public finance report (December). In this report, attention will center on the final public balance figures for 2018, particularly to evaluate if fiscal targets are accomplished. It should be noted that the public deficit target (as measured by the PSBRs) stands at 2.5% of GDP. As far as November, data shows a 1.5% deficit, equivalent to MXN\$351.0bn. In addition, attention will focus on the final revenue and spending figures, especially when compared to the original MoF estimates within the 2018 Budget and considering changing dynamics, such as in the price of the crude oil mix, the exchange rate, as well as interest rates. Finally, we will also look into public debt figures, which as of November stands at 44.5% of GDP, marginally below the year-end forecast of 45.3% (as measured by the HBPSBRs).

Banking credit will show a 6.4% yoy increase in December. It is our take that credit to the non-financial sector continued flowing in the twelfth month of the year. In particular, we estimate a 6.4% yoy expansion in banking credit to the private, non-financial sector (in real terms), as a result of a 1.6% increase in consumer credit, coupled with a 4.6% and 9.7% expansion in mortgages and corporate credit, in the same order.

Remittances to remain strong in December. We expect remittances in the last month of last year at US\$ 3,005.9 million (+8.5% yoy). In annual terms and based on this forecast, remittances would stand an inch above US\$ 33.5 billion, an implied yearly growth rate of 10.7%. For the sake of comparison and as of November 2018, the YTD flow of remittances was already 3.1x higher than net inflows from tourism, making it one of Mexico’s top sources of foreign currency.

In the monthly dynamic, we observed a seasonally favorable effect from the holiday season, which tends to increase inflows during the month. Excluding the latter, we expect remittances to stay resilient despite some signs of deceleration in US economic activity. It is worth noting that employment data for Mexican migrants is not available due to the shutdown. The most recently release figures show that employment levels in this group stayed strong despite some weakness at the margin. Nevertheless, we believe the latter would be more than compensated by two factors. First, the average amount sent by migrants has picked up meaningfully at least since March 2018. In our view, this has been at least partially driven by the renewed uncertainty faced due to the anti-immigration rhetoric of the US administration, which remains in the spotlight with the current debate for the construction of the Wall at the Northern Border. Second, the USD/MXN exchange rate remained at relatively high levels in spite of the appreciation observed during the month, with an average level of 20.11 per dollar, below the 20.26 in November but much higher than the YTD average of 19.24 pesos per dollar.

Family remittances



Source: Banxico

Banxico’s survey of economic expectations. As usual, market focus will center on inflation forecasts. The median for 2019 stands at 3.89%, above our 3.5% forecast. Moreover, the medium-term estimates remain above target, standing at 3.6%. In addition, estimates for the reference rate will also be published. Our expectation is for Banxico to remain on hold at 8.25% at least during the first half of 2019.

Moreover, forecasts for GDP will also be published. In the last survey, economists expected growth in 2018 at 2.1%, in line with our forecast. For 2019, it was revised down from 1.9% to 1.8%, in line with our estimate. Finally, regarding the exchange rate, we could see a marginal revision, considering that the YE19 forecast stands at USD/MXN 20.30 (Banorte: 21.30).

PMI indices to weaken on fuel distribution challenges. We expect PMI indices to feel the brunt of the delay in fuel distribution in several states during the month, which is likely to impact heavily in the “deliveries” component. On the contrary, some companies could have benefitted from tax cuts in the Northern Border. Despite the uncertainty about the impact of these changes, it is our take that sentiment was less optimistic due to the immediate constraints imposed by the first factor, along its scope in terms of geographical range.

Specifically, we believe the manufacturing PMI could show the most impact, at 48.5pts, 0.7pts lower than December and its third consecutive month in contraction territory. In our view, apart from the abovementioned factor, this sector is facing global challenges mainly due to trade tensions, in particular between the US and China, which is likely to impact Mexico due to the highly integrated nature of supply chains. In this respect, the US ISM and PMI manufacturing indices in December saw hefty declines. Moreover, weakness among businessmen seems to be concentrated in this sector according to confidence surveys, with all sub-indices declining in December.

Going to the non-manufacturing index, we estimate a 0.4pts decrease to 49.0pts. We believe that the retail sector could be the most impacted, although less than the manufacturing component. In this respect, business confidence in this sector held up relatively stronger in December, increasing strongly in the investment component. Nevertheless, two potential headwinds could be: (1) The recently enacted minimum wage increase; and (2) higher unemployment, as shown by the strong uptick in the unemployment rate to a two-year high in December 2018.

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HOLD	<i>When the share expected performance is similar to the MEXBOL estimated performance.</i>
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GRUPO FINANCIERO BANORTE S.A.B. de C.V.
Research and Strategy

Gabriel Casillas Olvera	Chief Economist and Head of Research	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godínez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967

Economic Analysis

Delia María Paredes Mier	Executive Director of Economic Analysis	delia.paredes@banorte.com	(55) 5268 - 1694
Katia Celina Goya Ostos	Senior, Global Economist	katia.goya@banorte.com	(55) 1670 - 1821
Juan Carlos Alderete Macal, CFA	Senior Economist, Mexico	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Miguel Alejandro Calvo Domínguez	Economist, Regional	miguel.calvo@banorte.com	(55) 1670 - 2220
Francisco José Flores Serrano	Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611

Fixed income and FX Strategy

Alejandro Padilla Santana	Head Strategist – Fixed income and FX	alejandro.padilla@banorte.com	(55) 1103 - 4043
Santiago Leal Singer	FX Senior Strategist	santiago.leal@banorte.com	(55) 1670 - 2144
Leslie Thalia Orozco Vélez	Fixed Income and FX Strategist	leslie.orozco.velez@banorte.com	(55) 5268 - 1698

Equity Strategy

Manuel Jiménez Zaldivar	Director Equity Research — Telecommunications / Media	manuel.jimenez@banorte.com	(55) 5268 - 1671
Victor Hugo Cortes Castro	Technical Analysis	victorh.cortes@banorte.com	(55) 1670 - 1800
Marissa Garza Ostos	Equity Research – Conglomerates / Financials/ Mining / Petrochemicals	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Equity Research – Airlines / Airports / Cement / Infrastructure / REITs	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Equity Research – Auto Parts/ Consumer Discretionary / Real Estate / Retail	valentin.mendoza@banorte.com	(55) 1670 - 2250
Francisco Duarte Alcocer	Analyst	francisco.duarte.alcocer@banorte.com	(55) 1103 - 4000 x 2707
Jorge Antonio Izquierdo Lobato	Analyst	jorge.izquierdo.lobato@banorte.com	(55) 1670 - 1746
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251

Corporate Debt

Tania Abdul Massih Jacobo	Director Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior, Corporate Debt	hugo.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248

Wholesale Banking

Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(55) 1670 - 1889
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.cebillos@banorte.com	(55) 5268 - 9996
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Gerardo Zamora Nanez	Head of Transactional Banking, Leasing and Factoring	gerardo.zamora@banorte.com	(81) 8318 - 5071
Jorge de la Vega Grajales	Head of Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Head of Private Banking	luis.pietrini@banorte.com	(55) 5004 - 1453
René Gerardo Pimentel Ibarrola	Head of Asset Management	pimentelr@banorte.com	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Head of International Banking	rvelazquez@banorte.com	(55) 5004 - 5279
Victor Antonio Roldan Ferrer	Head of Corporate Banking	victor.rolan.ferrer@banorte.com	(55) 5004 - 1454